

Message Text

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PAGE 01 STATE 043979
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FM SECSTATE WASHDC

TO AMEMBASSY ABU DHABI

AMEMBASSY DOHA

AMEMBASSY JIDDA

AMEMBASSY KUWAIT

AMEMBASSY MANAMA

AMEMBASSY MUSCAT

C O N F I D E N T I A L STATE 043979

FOLLOWING REPEAT ABU DHABI 419 SENT ACTION SECSTATE INFO TEHRAN
FEB 14.

QUOTE C O N F I D E N T I A L ABU DHABI 0419

E.O. 11652: GDS

TAGS/ ENRG, TC

SUBJ: TAX AND ROYALTY PROBLEMS FOR CRESCENT PETROLEUM

REF: ABU DHABI A-8

1. SUMMARY: GENERAL MANAGER OF CRESCENT PETROLEUM, WHICH
OPERATING MUBARRAQ FIELD NEAR ISLAND OF ABU MUSA, HAS INFORMED
AMBASSADOR THAT TAX AND ROYALTY PROBLEMS FACED BY CRESCENT
RAPIDLY COMING TO A HEAD. JOHN BORETA, PRESIDENT OF BUTTES
(OPERATOR OF CONCESSION) WILL BE CONTACTING NEA AND EB
OFFICIALS FEB. 14 TO SEEK USG INTERVENTION WITH GOVERNMENT
OF SHARJAH AND NATIONAL IRANIAN OIL CONSORTIUM (NIOC) TO PREVENT
APPLICATION OF ONEROUS FISCAL TERMS WHICH WOULD FORCE CRESCENT
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PAGE 02 STATE 043979

TO TERMINATE OPERATIONS AND COULD RESULT IN NASTY LEGAL ISSUES.
END SUMMARY.

2. ON FEBRUARY 12, HAMID JAAFAR MET WITH ME TO REVIEW IN DETAIL
HISTORY OF TAX AND ROYALTY PROBLEM CRESCENT PETROLEUM HAS HAD
FOR ITS CONCESSION OFF ABU MUSA ISLAND. CONVERSATION REPORTED
IN DETAIL IN REF AIRGRAM, WHICH SHOULD REACH DEPARTMENT EARLY

NEXT WEEK. BRIEFLY, ISSUE IS THAT AT TIME BUTTES NEGOTIATED PROTOCOL WITH SHARJAH IN 1971, TAX AND ROYALTY RATES SET AT 55 AND 12.5 PERCENT RESPECTIVELY, WHICH WERE THEN PREVAILING OPEC CONCESSIONARY TERMS. ONCE PRODUCTION UNDERWAY IN 1974, NIOC, WHICH SHARES HALF OF OIL REVENUE DERIVED FROM FIELD (FOLLOWING ESTABLISHMENT IRANIAN CO-SOVEREIGNTY OVER ABU MAUSA ISLAND IN 1971), BEGAN PRESSING SHARJAH TO RAISE TAX AND ROYALTY. PRESSURE INTENSIFIED IN LATE 1974 AFTER OPEC HAD ESTABLISHED NEW "ABU DHABI FORMULA" OF 85 PERCENT TAX AND 20 PERCENT ROYALTY.

3. AFTER MUCH SPARRING, CRESCENT THOUGHT IT HAD BEEN ABLE TO CONVINCE SHARJAH, WHICH ADMINISTERS CONCESSION UNDER TERMS OF 1971 PROTOCOL, THAT THERE NO ECONOMIC BASE FOR CHANGE IN TAX AND ROYALTY. CRESCENT HAD PROVIDED INFORMATION TO SHARJAH AND SEPARATELY NO NIOC THAT FIELD IS MARGINAL (BUTTES ESTIMATES ONLY 60 MILLION BBLs RECOVERABLE, NIOC ESTIMATES 75 MILLION BBLs), THAT DEVELOPMENT COSTS MUCH HIGHER THAN EARLIER ANTICIPATED BECAUSE OF DIFFICULT GEOLOGY, AND THAT PROTOCOL REQUIRED THAT ANY CHANGE TO BENEFIT OF SHARJAH REQUIRED BOTH COMPANY AND SHARJAH GOVT TO DETERMINE IF CHANGE EQUITABLE TO BOTH PARTIES AND IF COMPANY CAN AFFORD IT, GIVEN SHARJAH'S ECONOMIC SITUATION. DESPITE NIOC OBJECTIONS, RULER OF SHARJAH HAD ACCEPTED THESE ARGUMENTS AND WROTE AMERICAN COMPANY LETTER IN JUNE 1975 SAYING THERE WOULD BE NO CHANGE IN FISCAL TERMS.

4. THIS SITUATION CONTINUED UNTIL AUGUST 1977 WHEN CRESCENT
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PAGE 03 STATE 043979

INFORMED RULER OF SHARJAH PROPOSED INCREASE IN TAX AND ROYALTY TO 66.66 AND 14.5 PERCENT RESPECTIVELY TO BE RETROACTIVE TO JULY 1975. STEP TAKEN BY SHARJAH AT NIOC'S URGING. CRESCENT HAD REPLIED THAT IT COULD NOT ACCEPT RETROACTIVITY WHICH WOULD COST COMPANY \$30 MILLION BUT COULD ACCEPT NEW TAX AND ROYALTY RATES. CRESCENT SUBSEQUENTLY LEARNED THAT NIOC INSISTING ON 77 PERCENT TAX AND 14.5 PERCENT ROYALTY RETROACTIVE TO JULY 1975. IN DECEMBER 1977, BORETTA VISITED SHARJAH AND AGREED CONSIDER HIGHER TAX AND ROYALTY DEMANDED BY NIOC BUT WITH NO RETROACTIVITY. WHEN NIOC DISAGREED, RULER OF SHARJAH APPARENTLY HAD WRITTEN AMOUZEGAR SAYING IRANIANS UNREASONABLE AND THAT WOULD CAUSE CRESCENT TO MOVE OUT. NIOC'S REACTION APPARENTLY HAD BEEN THAT CRESCENT HAD TRIED BAMBOOZLE SHARJAH AND IF IT DID NOT AGREE, NIOC WOULD TAKE OVER OPERATION OF FIELD ITSELF.

5. ON FEBRUARY 7, BERETA WAS CALLED BACK TO SHARJAH AND WAS TOLD BY RULER THAT HE WANTED TAX AND ROYALTY TO BE 77 PERCENT AND 14.5 PERCENT RESPECTIVELY AND PAYMENT MADE RETROACTIVE TO JANUARY 1, 1977. COMPANY ESTIMATES THIS WOULD COST IT \$12 MILLION. CRESCENT DID NOT KNOW IF THESE TERMS ACCEPTABLE TO NIOC BUT BORETTA TOLD BY RULER OF SHARJAH THAT NIOC PREPARED TO STOP CRESCENT OPERATION OF FIELD AND TAKE OVER OPERATION. WHILE

BORETA BELIEVED HE HAD TIME RETURN TO US TO DISCUSS ISSUE WITH SHAREHOLDERS, JAAFR SAID HE HAD REASON BELIEVE RECENT CONTACTS BETWEEN IRANIAN AMBASSADOR AND SHARJAH RULER HAD BROUGHT MATTER TO A HEAD AND THAT CRESCENT WOULD BE OFFICIALLY INFORMED IN NEXT FEW DAYS THAT THESE ARE TERMS, TAKE IT OR LEAVE IT. JAAFAR SAYS THAT CRESCENT STILL HAS \$50 MILLION INVESTED IN FIELD WHICH IT HAS NOT AMORTIZED. MOREOVER, IT UNCERTAIN WHAT TO DO REGARDING DRILLING NOW UNDERWAY IN NEW FIELD IN CONCESSION AREA. CRESCENT FEELS THAT IF NEW TAX AND ROYALTY RATE APPLIED RETROACTIVELY TO JANUARY 77, IT CAN NO LONGER REMAIN IN SHARJAH. IT ALSO FEARS THAT ITS CLAIM FOR \$50 MILLION NET VALUE AS COMPENSATION IF FORCED TO LEAVE MAY BE WASHED OUT BY SHARJAH AND NIOC THEN INSISTING ON MAKING TAX AND ROYALTY PAYMENTS RETROACTIVE TO 1975.

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PAGE 04 STATE 043979

6. COMMENT: WHILE WE ARE NOT IN POSITION VERIFY ALL OF JAAFAR'S STATEMENTS, CRESCENT PULL OUT AT THIS TIME WOULD HAVE VERY SEVERE IMPACT ON SHARJAH'S ECONOMY WHICH ALREADY SUFFERING FROM DEPRESSED ECONOMIC CONDITIONS IN NORTHERN EMIRATES AND OVER BUILDING IN ANTICIPATION OF HIGHER OIL REVENUES AND GREATER PRIVATE CAPITAL INFLOWS. SHOULD NIOC TRY TO TAKE OVER CRESCENT OPERATION, IT WOULD REKINDLE POLITICAL PROBLEMS IN GULF WHICH OCCURRED IN 1971 WHEN IRAN OCCUPIED TUNBS AND INSISTED ON CO-SHARING ISLAND OF ABU MUNSA WITH SHARJAH. I ANTICIPATE CRESCENT WILL SEEK DEPARTMENT INTERVENTION FOR EMBASSY ABU DHABI TO MAKE DEMARCHE WITH SHARJAH AGAINST APPLICATION ONEROUS FISCAL TERMS AND FOR EMBASSY TEHRAN TO GET NIOC TO RELAX ITS PRESSURES ON SHARJAH. DICKMAN UNQUOTE VANCE

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